No. 17-419

IN THE

Supreme Court of the United States

JAMES DAWSON AND ELAINE DAWSON,

Petitioners,

v.

DALE W. STEAGER, AS STATE TAX COMMISSIONER OF WEST VIRGINIA,

Respondent.

On Petition For Writ Of Certiorari To The Supreme Court Of Appeals Of West Virginia

REPLY IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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INTRODUCTION

The petition established that under this Court's decisions in *Davis v. Michigan Department of Treasury*, 489 U.S. 803, 815-16 (1989), and *Jefferson County, Alabama v. Acker*, 527 U.S. 423 (1999), a state may not impose a heavier tax burden on federal employees than state employees when there are no "significant differences between the two classes." The decision below erroneously departed from this rule by imposing a heavier tax burden on Mr. Dawson than on similarly situated state law-enforcement personnel, and deepened a circuit conflict in the process. The petition also showed that lower courts are struggling with the contours of the intergovernmental tax immunity doctrine and have come to conflicting positions on related issues under this doctrine. These struggles, potentially affecting millions of retirees, will continue without this Court's intervention.

In its Opposition, Respondent does not deny that *Davis* and *Jefferson County* control the outcome here, or that Mr. Dawson's job description is similar to those of the more favorably treated West Virginia state retirees, or that the West Virginia Circuit Court stated that such similarity was "undisputed." Nor does Respondent deny that the tax scheme at issue was intentionally designed to favor certain state retirees over all other retirees. Respondent also does not deny that several courts have followed the prior West Virginia decision in *Brown v. Mierke*, 443 S.E.2d 462 (W. Va. 1994), to reach rulings similar to the one at issue here, or that a ruling from this Court in this case would have far-reaching implications.

Rather, Respondent makes one overarching argument in response – that under *Davis* and *Jefferson County* – a state's less favorable treatment of federal retirees than similarly situated state retirees is permissible so long as the state does not adopt a "blanket" rule favoring state retirees, but rather discriminates only in favor of certain small, subclasses of state retirees. It then urges that this rule explains the conflict in authority in the state courts and suggests that rejecting this narrow discrimination rule would cause a substantial amount of litigation, that it characterizes as unnecessary.

Respondent's argument, however, is plainly wrong under *Davis* and *Jefferson County*. Those cases make clear that, even where the subclasses of employees are small (indeed, in *Jefferson County*, the Court addressed taxes on sitting judges), it is impermissible to treat a class of state employees or retirees more favorably than a similarly situated class of federal employees or retirees.

Once Respondent's fundamental and erroneous reading of *Davis* and *Jefferson County* has been exposed, its other arguments fall away. There is in fact a real conflict between those state courts that faithfully follow this Court's intergovernmental tax immunity cases and those that apply West Virginia's incorrect view as expressed in *Brown*. And the effect of this Court's intervention to correct the ruling below would indeed be widespread, but would be salutary rather than pernicious.

This Court's intervention is warranted.

ARGUMENT

I. *DAVIS* AND *JEFFERSON COUNTY* ESTABLISH THAT A STATE CANNOT TREAT GROUPS OF STATE RETIREES MORE FAVORABLY THAN SIMILARLY SITUATED GROUPS OF FEDERAL RETIREES

1. In *Davis*, this Court very clearly held that "the imposition of a heavier tax burden on those who deal with one sovereign than is imposed on those who deal with the other" must be justified by demonstrating that the disparate treatment is the result of "significant differences between the two classes." 489 U.S. at 815-16. The Court expressly rejected the state's rationale that it had a legitimate interest in hiring qualified civil servants, noting that it was "beside the point," because it was a *reason for* the preferential treatment of state employees, not a *significant difference* between state and federal employees. *Id.*

In *Jefferson County*, this Court reiterated that "a state tax exempting retirement benefits paid by the State but not those paid by the Federal Government" violates the doctrine of intergovernmental tax immunity. 527 U.S. at 442. That case involved the question whether a county could charge an occupational tax on federal judges where the tax generally applied to all persons working within the county who were not otherwise required to pay a license fee under state law. The Court held that, even though some state judges did pay a license fee rather than the tax, the tax was permissible because it did not "discriminate against federal judges in particular, or federal officeholders in general, based on the federal

source of their pay or compensation." *Id.* at 442-443. However, the Court cautioned—"[s]hould Alabama or Jefferson County authorities take to exempting state officials while leaving federal officials (or *a subcategory of them*) subject to the tax, that would indeed present a starkly different case" violating the doctrine of intergovernmental tax immunity. *Id.* at 443 (emphasis added).

2. Respondent claims that *Davis* and *Jefferson County* forbid only a blanket tax exemption for state employees or retirees, but not a narrow one, even where similarly situated federal employees or retirees are treated less favorably. Opp. 25-26. This argument cannot be squared with the actual holdings and language of those cases.

First, both *Davis* and *Jefferson County* contain express language that defeats Respondent's argument. *Davis* plainly states that discrimination between classes of state and federal employees or retirees could be justified only by "significant differences between the two classes." 489 U.S. at 816-17. And *Jefferson County* stated that it would be impermissible to "discriminate against federal judges in particular, or federal officeholders in general." 527 U.S. at 442-443.[1] Thus, the Court expressly stated that not only

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[1] Respondent invokes the Court's description in *Jefferson County* of the "narrow approach" and "tight limits this Court has set" for the doctrine of intergovernmental tax immunity. Opp. 26-27 (quoting 527 U.S. at 436-37). But that language was simply used to distinguish the Eleventh Circuit's holding and historical practices that prevented any form of state taxation on the income of federal employees from the modern doctrine that prohibits only "discriminat[ory]" taxation. 527 U.S.

blanket exemptions, but exemptions favoring subclasses of state employees or retires over federal employees or retirees are impermissible.

Second, while *Davis* did involve a blanket state exemption, nothing in that case indicates that it is limited to such exemptions, and in fact, the language of the case plainly establishes the contrary. *Jefferson County*, on the other hand, did involve a much narrower tax and exemption and made clear that if such a narrow exemption discriminated against a subclass of similarly situated federal employees, it would be invalid. *Id.* There is no persuasive rationale that would support Respondent's reading. The crux of the intergovernmental tax immunity doctrine is to prevent discrimination based on the "federal source" of compensation. *Id.* at 443. But such prohibited discrimination is present whether there is blanket discrimination or more narrow discrimination against federal employees treated less favorably than similarly situated state employees.

Third, Respondent's argument in this regard, if anything, resembles the position of the dissent in *Davis*, which the rest of the Court expressly rejected. The dissent emphasized that the exemption applied only to 130,000 retired state employees out of 4.5 million individual taxpayers and urged that "[t]he fact that a State may elect to grant a preference, or an exemption, to a small percentage of its residents does not make the tax discriminatory in any sense

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(continued...)

at 436. It does not support Respondent's argument that "narrow" discriminatory state taxation is acceptable.

that is relevant to the doctrine of intergovernmental tax immunity." 489 U.S. at 821 (Stevens, J., dissenting). But that reasoning was rejected by the Court in *Davis*, and it cannot carry the day here.

3. Stripped of its erroneous reading of *Davis* and *Jefferson County*, Respondent has no meaningful defense of the decision below. Respondent suggests that the differential tax treatment at issue is not "discriminatory." Opp. 28-29. However, it ignores Respondent's concession in the circuit court that the purpose of the state exemption was to "benefit the narrow class of state law enforcement officers" listed in the statute. Pet.App.23a. The circuit court thus found that the inconsistent tax treatment was "unquestionably based on the source of one's retirement income and precisely the type of favoritism the doctrine of intergovernmental tax immunity prohibits." *Id.* Neither the West Virginia Supreme Court's nor Respondent's wishful recharacterization of the statutory scheme changes that reality.

Respondent also notes that it urged in the West Virginia Supreme Court that there may be "other significant" differences between the class of state retirees that benefit from the exemption and federal retirees such as Mr. Dawson. Opp. 29. But it concedes, as it did in the circuit court, that there are "substantial similarities" in their job descriptions. *Id.*; *see also* Pet.App.22a. (circuit court emphasizing that it is "undisputed" that "there are no significant differences between Mr. Dawson's powers and duties as a U.S. Marshal and the powers and duties of the state and local law enforcement officers listed in [Section 12(c)(6)].").

In short, West Virginia gives preferential tax treatment to a substantial category of state law-enforcement retirees, but does not treat as favorably a similarly situated class of federal law-enforcement retirees. This is forbidden by this Court's precedents, and the decision below warrants review.

II. RESPONDENT FAILS TO REFUTE PERSUASIVELY THE CONFLICT IN THE LOWER COURTS

The petition showed that state courts conflict over their treatment of the intergovernmental tax immunity doctrine, with several faithfully applying this Court's precedents to strike down discriminatory state taxation schemes and others following the West Virginia Supreme Court's prior decision in *Brown* to permit such schemes. Respondent imports its untenable blanket exemption/narrow class distinction in an attempt to explain these cases. But like its mischaracterization of this Court's precedent, this explanation fails.

1. The Supreme Courts of Arkansas, Colorado and Missouri hold that state taxation schemes that treat state employees or retirees more favorably than similarly situated federal employees or retirees are impermissible.

a. **Arkansas.** In *Pledger v. Bosnick*, 811 S.W.2d 286, 288 (Ark. 1991), *abrogated on other grounds by State, Dep't of Fin. & Admin. v. Staton*, 942 S.W.2d 804, 806 (Ark. 1996), the court struck down a scheme that fully exempted retirement income received by retirees from the Arkansas Public Employees, Teachers, State Highway Police, and State Highway Employees Retirement Systems, while allowing only a

$6,000 exemption for all other retirees. The court held that "the tax discriminate[d] based upon the source of the payment," because state retirees were exempted and similarly situated federal employees were not. 811 S.W.2d at 292.

Respondent argues that because the question in *Pledger* was whether the discrimination was based on the source of the income, the court's failure to discuss any difference between blanket and narrow exemptions is unsurprising. Opp. 12-14. But *Pledger* was not a blanket exemption case. Only certain specific state retirement programs were at issue, just as here. *See, e.g., Landers v. Stone*, 496 S.W.3d 370 (Ark. 2016) and *Rothbaum v. Arkansas Local Police & Fire Ret. Sys.*, 55 S.W.3d 760 (Ark. 2001) (describing other programs). And *Pledger* did not mention any distinction between discriminatory blanket and narrow exemptions. Its reasoning, therefore, is contrary to that of the West Virginia Supreme Court and the other courts to have adopted similar reasoning.

b. **Colorado**. *Kuhn v. State Department of Revenue of State of Colorado*, 817 P.2d 101, 103 (Colo. 1991) (en banc), similarly struck down a taxing scheme that discriminated in favor of state retirees and against federal military retirees. The court explained that Davis "prohibit[s]" taxes "that discriminate between state and federal workers based on the source of the income" unless the inconsistent treatment is justified by significant differences between the classes. *Id.* at 107 (citing *Davis*, 489 U.S. at 816). The court said nothing to indicate that the holding in Davis is limited to blanket tax exemptions.

Respondent again argues that it is not surprising that *Kuhn* did not mention any significance of the "blanket" nature of the state exemption. Opp. 14-16. But if the court in *Kuhn* had either adopted a blanket/narrow exemption distinction or reasoned that *Davis* made such a distinction, surely it would have mentioned it in its decision.

c. **Missouri.** In *Hackman v. Director of Revenue*, 771 S.W.2d 77, 79 (Mo. 1989), the court followed *Davis* to invalidate several statutory exemptions for subgroups of state retirees that did not similarly exempt federal retirees. Respondent seizes upon the court's language that "[t]he effect of Missouri's scattered retirement benefit [exemption] statutes is identical to that of Michigan's exemption statute for purposes of a *Davis* analysis." Opp. 16-17 (quoting *Hackman*, 772 S.W.2d at 80). But, it is not clear that the court meant that aggregating the subgroups in the different listed exemptions created a blanket exemption. Rather, the court emphasized that the state exemptions had the legal effect of a violation of the intergovernmental tax immunity doctrine. In any event, *Hackman* certainly did not adopt or mention any blanket/narrow exemption distinction.

2. Conversely, several courts have upheld discriminatory state taxation schemes following *Davis*.

a. **West Virginia.** In *Brown*, the West Virginia Supreme Court rejected a challenge by federal military retirees, who claimed that they were entitled to tax exemptions provided to certain allegedly similarly situated state retirees. 443 S.E.2d 462. The decision below followed *Brown*, rather than this Court's decision in *Davis*. Pet. 5-6.

Respondent concedes that "neither *Brown* nor the decision below turned on a finding that discriminatory tax treatment was 'justified by significant differences between the two classes of employees.'" Opp. 20 (quoting *Davis*, 489 U.S. at 815). Respondent urges that such a justification was not necessary because the tax schemes did not impermissibly discriminate on the basis of the source of the federal retirees' income. Opp. 20. But that argument just repeats the erroneous blanket/narrow exemption distinction that the court below originally adopted in *Brown* and repeated in this case. That distinction conflicts with this Court's rulings and the rulings of the Arkansas, Colorado and Missouri Supreme Courts. *Brown* has been adopted by the courts of other states, further cementing the conflict this Court should reconcile.

b. **New Mexico.** In *Alarid v. Secretary of N.M. Department of Taxation and Revenue*, 878 P.2d 341, 343 (N.M. Ct. App. 1994), the court rejected the challenge of retirees from Los Alamos National Laboratory whose retirement income, paid by the University of California through a federal contract, was taxed differently from that of retirees from other New Mexico educational institutions. The court followed *Brown*, reasoning that granting narrow tax exemptions to state employees does not pose the same concerns as the blanket exemptions struck down in *Davis*: "[t]he fact that the State has chosen to exempt from state tax one limited class of state retirees does not mean Plaintiffs are being illegally discriminated against." *Id.* at 347 (citing *Brown*, 443 S.E.2d at 462).

Respondent is correct that this decision is from the New Mexico Court of Appeals (it was inadvertently

misidentified in the Petition), Opp. 20-21, but Respondent points to no decision from the New Mexico Supreme Court contradicting it; and that court denied certiorari in *Alarid*, and could have reviewed that decision if it determined it to be erroneous. Respondent's other argument, that the retirement funds, while owned by the federal government, were paid by California, *id.* is a distinction without a difference. As part of its holding, the court analyzed whether plaintiffs were discriminated against because of the affiliation of their retirement funds with the federal government and reasoned that they were not, based upon *Brown*. That the court addressed other principles also applicable in this particular case does not negate that holding.

c. **Massachusetts**. In *Cooper v. Commissioner of Revenue*, 658 N.E.2d 963, 963 (Mass. 1995), the Massachusetts Supreme Court likewise followed *Brown* to uphold state tax exemptions for certain state employees that did not extend to similarly situated federal employees. It reasoned that because the tax provision at issue favored a "small and dwindling class" of state retirees, it could not constitute "discrimination against federally funded benefits." *Id.* at 965 (citing *Brown*, 443 S.E.2d at 462; *Alarid*, 878 P.2d at 341).

Respondent urges that the decision was based on the date of hire and the occupation of the exempted state retirees, Opp. 22-23, but the exemption did not apply to similarly situated federal retirees regardless of their date of hire. Thus, by definition, it discriminated based on the source of the retirement funds. *Cooper* thus shows the erroneous expansion of *Brown*.

3. Respondent does not dispute conflicts in the state courts regarding related issues involving similar arguments to circumvent this Court's rulings in *Davis* and *Jefferson County*. Pet. 21-25. Rather, Respondent asserts that the presence of these cases actually undermines the case for review here. Opp. 23-25. To the contrary, those cases plainly demonstrate the confusion in the lower courts over the proper interpretation of this Court's rulings. Moreover, resolution of the core issue presented in this case would help resolve this confusion. If the blanket/narrow class distinction is struck down or clarified, the lower courts would be far better able to appropriately address these related issues.

III. THIS CASE PRESENTS AN IDEAL VEHICLE TO DECIDE THIS IMPORTANT AND RECURRING QUESTION

1. Respondent does not deny that there is a great deal of litigation in the state courts over the question presented and similar issues. Rather, Respondent asserts that granting review would create additional, unnecessary litigation. Opp. 29-33. But the reality is that clarification of this Court's previous rulings would increase certainty and likely lead to the elimination of taxation schemes designed to circumvent those rulings. To the extent any additional litigation is generated, it would be with the purpose of eliminating impermissible discrimination in taxation. That is a salutary outcome.

2. Respondent also suggests that because this Court denied certiorari in *Brown* in 1994, it should do so here. Opp. 27. But that ignores the role *Brown* has played since then in making mischief and lead-

ing to erroneous results like that below. Again, this favors review.

CONCLUSION

The petition should be granted. Alternatively, because the decision below is so plainly contrary to this Court's precedent, summary reversal is warranted.

Respectfully submitted,

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